[HIGH COURT OF AUSTRALIA.]

A. & S. RUFFY PROPRIETARY LIMITED . APPELLANT;

AND

FEDERAL COMMISSIONER OF TAXATION . RESPONDENT.

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MELBOURNE, *Mar.* 5, 6;

SYDNEY, *April* 30.

Dixon C.J. Williams, Webb, Fullagar and Taylor JJ.

Income Tax (Cth.)—Allowable deduction—Income of co-operative company distributed among shareholders as dividends—Co-operative company defined as "Company the rules of which limit the number of shares which may be held by" "any one shareholder" and "is established for the purpose of carrying on any business having as its primary object . . ."—Limitation on shareholding—What constitutes—Primary object—Whether to be considered only by reference to memorandum of association—Necessity for purpose of business to supply shareholders with services etc.—Whether necessary for class of shareholders for whom services rendered to be co-extensive or of same class of shareholder as class among which distribution of dividend made—Income Tax and Social Services Contribution Assessment Act 1936-1950 (*No.* 27 *of* 1936—*No.* 48 *of* 1950), *ss.* 117-120.

Section 117 of the *Income Tax and Social Services Contribution Assessment Act* 1936-1950 sets out various requirements which a company must meet in order to be a co-operative company. One requirement is that the rules of the company limit the number of shares which may be held by, or by and on behalf of, any one shareholder. Section 117 also requires that the company be established "for the purpose of carrying on any business having as its primary object or objects one or more of the following:— . . . (b) the acquisition of commodities or animals from its shareholders for disposal or distribution; (c) the storage, marketing, packing or processing of commodities of its shareholders".

Section 118, so far as material, provides that if, in the ordinary course of business of a company in the year of income, the value of commodities and animals acquired by it from its shareholders is less than ninety per cent of the total value of commodities and animals acquired by it, that company shall in respect of that year be deemed not to be a co-operative company. Section 120 (1) provides, inter alia, that so much of the assessable income of a co-operative company as is distributed among its shareholders as interest or dividends on shares shall be an allowable deduction.

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The appellant company carried on the business of manufacturing sausage casings from sheep's intestines known as "runners". The company had an authorised share capital of £10,000 divided into 10,000 £1 shares and the company's articles provided that no number of shares in excess of 5,000 should be held by or on behalf of any one shareholder. The memorandum of association contained the customary heterogeneity of objects. By the articles of association the 10,000 £1 shares were divided into three classes, viz. 8,000 A-class shares of £1, 1,000 B-class shares of £1 and 1,000 C-class shares of £1.

During the year of income ended 31st August 1951 the issued capital consisted of 5,760 A-class shares, 640 B-class shares and 635 C-class shares, each class having rights stated in the articles, and during that year the appellant company acquired more than ninety per cent of the total value of runners acquired by it from shareholders in the company, all such shareholders being holders only of C-class shares with the exception of one such shareholder who held 2,880 A-class shares. For that year of income a dividend of two hundred per cent was paid on the A- and B-class shares and a preference dividend of six per cent on C-class shares, so that out of the total amount of dividends, viz. £12,838, A- and B-class shareholders received £12,800 and C-class shareholders £38. In the notice of assessment for that year the respondent Commissioner included the total amount of the dividends in the appellant taxpayer's assessable income. The company contended that it was a co-operative company within the meaning of the Act and that the dividends were an allowable deduction under s. 120 (1).

Held :—that the primary object or objects of the business of the company could not be determined solely by reference to the memorandum of association ; and that when the history, constitution and activities of the company were looked at it was apparent that the primary object of the business for the carrying on of which the company was established was to earn profits for its A- and B-class shareholders, and, accordingly, the company was not a co-operative company within the meaning of Div. 9 of Pt. III of the Act.

Held, by *Dixon* C.J., *Williams*, *Webb* and *Fullagar* JJ. :—that the limitation on shareholding provided in the articles conformed with the requirement of s. 117.

By *Dixon* C.J., *Williams* and *Webb* JJ. that it was not necessary that the class of shareholders referred to in the lettered paragraphs of s. 117 should be co-extensive with the class among whom the distribution is made for which s. 120 (1) provides.

By *Fullagar* J. that par. (c) of s. 117 does not cover cases where the property in the commodity or the animal passes to the company ; and that there is no implication that every shareholder in the class of shareholders referred to in the lettered paragraphs of s. 117 must be a supplier of commodities or animals to the company and therefore the condition prescribed by s. 118 was fulfilled.

CASE STATED BY *Kitto* J.

A. & S. Ruffy Proprietary Limited appealed to the High Court from an assessment of income tax in respect of the year ended 31st August 1951. The appeal came on for hearing before *Kitto* J. who, on 11th November 1957, with the concurrence of the parties and pursuant to s. 198 of the *Income Tax and Social Services Contribution Assessment Act* 1936-1950 stated a case for the opinion of a Full Court of the High Court substantially as follows :—

2. Campbellfield Holdings Pty. Ltd. (hereinafter called " the old company ") was incorporated under the *Companies Acts* (Vict.) in 1933 under the name A. & S. Ruffy Pty. Ltd. From the date of its incorporation until 1st September 1949 the old company carried on the business of sausage casing manufacturers and suppliers. That business consists of the acquisition of sheep and lambs intestines from wholesale butchers (the only source of supply of such commodities) and of the manufacture of sausage casings therefrom and of the disposal of the same.

3. As at 30th June 1941 the issued capital of the old company consisted of 1,600 shares and the shareholding was as follows :—

A. W. Ruffy	370	"A" class shares
A. T. Ruffy	350	"A" class shares
Estate H. G. E. Ruffy	670	"A" class shares
H. G. E. Ruffy Jnr.	50	"A" class shares
Estate S. J. C. Ruffy	100	"B" class shares
Mrs. S. J. C. Ruffy	60	"B" class shares

4. During the year 1941 discussions were held between the old company and certain of the wholesale butchers from whom it obtained its supplies, namely, G. H. Townsend, G. F. Harris and N. L. Thompson. As a result of those discussions, agreement was reached for the allotment of shares in the old company to the said suppliers upon certain terms and conditions which were approved by the board of directors of the old company at a meeting on 28th October 1941. The agreement was duly entered into.

5. At a meeting of directors of the old company held on 2nd February 1942, it was reported that applications had been received from the said suppliers for shares as follows :—

G. H. Townsend	..	100 shares
G. F. Harris	..	75 shares
N. L. Thompson	..	45 shares

and that consent to the issue of the said shares had been refused by the Treasury under regulations made under the *National Security Act.*

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6. At an extraordinary general meeting of the old company held on 28th February 1946, a special resolution was duly passed amending the articles of association by making provision for " C " class shares.

7. At a meeting of the directors of the old company held on 28th February 1946, it was resolved that " C " class shares be allotted as follows :—

G. H. Townsend	..	170
N. L. Thompson	..	100
G. F. Harris	..	130
Total	..	400

8. At a meeting of the directors of the old company duly held on 9th December 1946, further " C " class shares were issued to wholesale butchers being suppliers of goods to the old company as follows :—

J. B. Dunn	..	100
Dench Brothers	..	50
M. C. Moog	..	50
P. Zmood	..	10

9. By not later than the year 1948 the old company was obtaining not less than 90% of its supplies from the " C " class shareholders referred to in pars. 6, 7, and 8 hereof. In the year 1949 the directors and shareholders of the old company decided to form a new company to carry on the business of acquiring sheeps and lambs intestines from the wholesale butchers from whom the old company acquired the same and of manufacturing sausage casings therefrom and of disposing of the same, that is to say to take over and carry on the business of the old company and that the shareholders in the old company should hold the same number of shares in the new company as in the old company.

10. At an extraordinary general meeting of the old company duly held on 23rd June 1949 an extraordinary resolution was passed changing its name to Campbellfield Holdings Pty. Ltd. On 19th July 1949 the Governor in Council duly approved of the said change of name pursuant to the provisions of the *Companies Act* 1938.

11. At a meeting of the holders of the "A" class shares in the old company duly held on 8th June 1949 it was resolved that the assets of the old company be sold to a new company. On the same day a meeting of " C " class shareholders was held for the purpose of dealing with the same matters but lapsed for want of a quorum and

it was decided to obtain their consent in writing to the proposed alteration of the articles.

12. At an extraordinary general meeting of the old company duly held on 20th July 1949 a special resolution was duly passed amending the articles of association of the old company as follows :— " THAT Article 4 of the Articles of Association of the Company be amended by adding at the end thereof the following namely :— ' Notwithstanding anything to the contrary contained or implied in the Articles of Association of the Company, in the event of any Company formed and incorporated in the State of Victoria (hereinafter called " the new Company ") acquiring the business and assets of this Company for a consideration of or including the allotment to this Company of the following fully paid up shares in the capital of the new Company namely—

"A" class shares in the capital of the new Company	2,875
"B" class shares in the capital of the new Company	320
"C" class shares in the capital of the new Company	635
	3,830

the following provisions shall (subject to the provisions of the *Companies Act* 1938) have effect in a winding up of this Company and the liquidator shall distribute the assets of the Company accordingly namely—

(i) Holders of "A" shares in this Company shall be entitled to receive and shall accept (pro tanto) in satisfaction of their interest in the Company's assets "A" class shares in the new Company equivalent in number to the "A" shares in this Company held by them.

(ii) Holders of " B " shares in this Company shall be entitled to receive and shall accept (pro tanto) in satisfaction of their interests in the Company's assets " B " class shares in the new Company equivalent in number to the " B " class shares in this Company held by them.

(iii) Holders of " C " class shares in this Company shall be entitled to receive and shall accept (pro tanto) in satisfaction of their interests in the Company's assets " C " class shares in the new Company equivalent in number to the " C " shares in this Company held by them.

(iv) All holders of shares in the Capital of this Company shall otherwise rank pari passu."

Consent in writing to the passing of the said special resolution was obtained from all the " C " class shareholders.

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13. A. & S. Ruffy Proprietary Limited (hereinafter called "the appellant") was incorporated under the *Companies Act* 1938 (Vict.) on 20th July 1949 as a company limited by shares and by a special resolution duly passed at a general meeting of the company on 20th July 1949 became a proprietary company pursuant to the said Act.

14. On 31st August 1949 the appellant entered into an agreement with the old company for the purchase of the business of casing manufacturers, formerly carried on by the old company.

15. At a general meeting of the shareholders of the old company duly held on 31st August 1949 it was resolved that the action of the directors in entering into the said agreement with the appellant for the sale of the old company's business be ratified. At a meeting of the directors of the appellant duly held on 31st August 1949 the said agreement was duly approved and it was resolved that the seal of the appellant be affixed thereto.

16. At the said meeting of directors of the appellant of 31st August 1949, it was resolved that the following shares be allotted to the old company pursuant to an application received—

"A" shares	.. 2,875	(shares numbered	6 to 2,880)
"B" shares	.. 320	(,, ,,	1 to 320)
"C" shares	.. 635	(,, ,,	1 to 635)

It was also resolved that the following transfers of "A" shares be approved—

J. A. L. Walsh to B. J. Dunn	..	1 share
B. Conabere to M. C. Moog	..	1 share
C. G. Landy to P. Zmood	..	1 share
H. G. E. Ruffy to William Dench and Steven Dench		1 share

17. The nominal capital of the appellant at all material times was £10,000 divided into 10,000 shares of £1 each which by the articles of association are divided into the following classes—

8,000 "A" class shares of One Pound Each
1,000 "B" class shares of One Pound Each
1,000 "C" class shares of One Pound Each

each class having the rights stated in the articles of association.

18. By a special resolution duly passed at a meeting of the old company duly held on 22nd February 1950 it was resolved that the old company be wound up voluntarily under the provisions of the *Companies Act* 1938, and that C. G. Landy be appointed liquidator for the purpose of such winding up.

19. At a meeting of the directors of the appellant duly held on 22nd February 1950 the following transfers of shares from the

liquidator of the old company were approved and the new shareholders duly entered in the share register of the appellant :—

Class "A"			
A5	Trustees of the Estate of the late H. G. E. Ruffy	1,340	6 –1,345
A6	H. G. E. Ruffy Jnr.	100	1,346 –1,445
A7	N. L. Thompson	1,435	1,446 –2,800
		2,875	
Class "B"			
B1	Alice Mona Ruffy as administratrix of Estate of S. J. C. Ruffy	320	1 –320
Class "C"			
C1	G. H. W. Townsend	170	1 –170
C2	G. F. Harris	130	171 –300
C8	N. L. Thompson	100	536 –635
C3	J. B. Dunn	100	301 –400
C4	H. Dench	50	401 –450
C5	M. C. Moog	50	451 –500
C6	F. J. Campbell	25	501 –525
C7	P. Zmood	10	526 –535
		635	

20. From 1st September 1949 and at all material times thereafter the appellant carried on the business of sausage casing manufacturers which it had acquired in the manner aforesaid.

21. At all times during the year ended 31st August 1951 the issued capital of the appellant consisted of 5,760 "A" class shares, 640 " B " class shares and 635 " C " class shares.

22. During the year ended 31st August 1951 the appellant in the ordinary course of its business acquired more than 90% of the total value of commodities acquired by it from shareholders in the appellant, namely from the following persons who held shares in the numbers and of the classes indicated opposite their names (each of such persons being a wholesale butcher)—

N. L. Thompson — 2,880 "A" class shares, 100 "C" class shares
M. C. Moog — 50 "C" class shares
G. F. Harris — 130 "C" class shares
P. Zmood — 10 "C" class shares
Dench Brothers — 50 "C" class shares
F. J. Campbell & Sons Pty. Ltd. — 25 "C" class shares
Howlett Bros. Pty. Ltd. — 10 "C" class shares
K. Gregory — 10 "C" class shares.

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23. On 7th December 1951 the annual general meeting of the appellant duly resolved that a dividend of 200% on the "A" and "B" class shares be paid from the profits of the year ended 31st August 1951 and that a preference dividend of 6% be paid on the "C" class shares from the profits of the year ended 31st August, 1951.

24. The said dividends were duly paid to the shareholders of the appellant, the total amount of dividends so paid being £12,838.

25. For the purposes of the *Income Tax and Social Services Contribution Assessment Act* 1936-1950 the appellant adopted as its accounting year the period of twelve months commencing on 1st September in each year and ending on 31st August in the next year. The appellant duly made a return of its income for the twelve months ending 31st August 1951 ; that return was based upon the appellant's profit and loss account for that period lodged with the return. The said return claimed as a deduction the amount of £12,838 being the said dividends from profits in respect of the year ended 31st August 1951. After an adjustment in respect of depreciation, the said return showed the taxable income of the appellant as £248.

26. By a notice of assessment dated 18th June 1953, the commissioner assessed the appellant for income tax in the sum of £4,170 17s. 0d. upon a taxable income of £13,231 in respect of its income for the year ended 31st August 1951. In making such assessment the commissioner included in the taxable income of the appellant for the year ended 31st August 1951, the sum of £12,838, which was described in the alteration sheet accompanying the said notice of assessment as—" Dividends claimed as a deduction under s. 120 have been disallowed as the company is not a co-operative company within the meaning of the provisions of s. 117 of the Act."

27. By notice of objection dated 7th August 1953 the appellant objected to the said assessment upon the following grounds :—

1. The said assessment is excessive and is wrong in fact and in law.

2. The commissioner was wrong in disallowing as a deduction the amount of £12,838 distributed among its shareholders as dividends on shares.

3. In the year of income the company distributed among its shareholders the amount of £12,838 as dividends on shares and such amount is an allowable deduction under s. 120 of the *Income Tax Assessment Acts*.

4. The commissioner was wrong in assessing the company to tax upon the basis that it is not a co-operative company within the

meaning of ss. 117 and 118 of the *Income Tax Assessment Acts* and should have assessed it as a co-operative company.

5. The company is and at all times material was a co-operative company within the meaning of ss. 117 and 118 of the *Income Tax Assessment Acts*.

28. By letter dated 1st October 1953 the commissioner disallowed the said objection to the assessment and by a letter dated 16th November 1953 the appellant requested the commissioner to treat the objection as an appeal and to forward it to the High Court of Australia. By a notice dated the 24th day of August 1956 the commissioner notified the appellant that on 24th August 1956 the said objection had been forwarded to the High Court of Australia at Melbourne.

29. The parties desire that the questions of law raised by the said appeal should be determined by the Full Court of the High Court and I accordingly state the following questions for the opinion of the Full Court—

(a) Am I bound to hold that the appellant was in respect of the year of income ended 30th August 1951 a " co-operative company " within the meaning of ss. 117 and 118 of the *Income Tax and Social Services Contribution Assessment Act* 1936-1950 ?

(b) Is it open to me to hold that the appellant was in respect of the said year of income a " co-operative company " within the meaning of ss. 117 and 118 of the *Income Tax and Social Services Contribution Assessment Act* 1936-1950 ?

(c) If the appellant was in respect of the said year of income a " co-operative company " within the meaning of ss. 117 and 118 of the *Income Tax and Social Services Contribution Assessment Act* 1936-1950 was the dividend amounting to £12,838 allowable as a deduction under s. 120 (1) of the said Act in respect of the said year of income ?

D. I. Menzies Q.C. (with him *K. A. Aickin*), for the appellant. In order to comply with s. 117 of the *Assessment Act* there must be a limitation on the number of shares in the company, a prohibition of quotation and the company must be established for the purpose of carrying on any business having as its primary object one of the matters set out. All that is necessary is a general limitation upon the number of shares which any shareholder may take. There is nothing which would require the limit to be so fixed that every

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member of the company could in fact have the full number limited. In looking to what is the primary object of the company's business the section is looking to the realities of the situation and not merely to the memorandum of association. "Its" in the words "its primary object" relates to the business and not to the company. It is not necessary under the section that the commodities should be acquired from all the shareholders; see by way of contrast s. 120 (1) (*c*). The dividend was declared and paid after the end of the financial year in which the amount of the dividend was claimed as a deduction. This is contemplated by ss. 117 et seq. which provide a special code for co-operative companies. If this was not so, a company might lose the benefit of the deduction by reason of the fact that it was no longer, in the year in which the dividend was declared, a co-operative company. In *Ardmona Fruit Products Co-operative Co. Ltd.* v. *Federal Commissioner of Taxation* (1) it was assumed, it is submitted wrongly, that unless the dividend was declared and paid in the year in question it could not be an allowable deduction.

L. Voumard Q.C. (with him *J. McI. Young*), for the respondent. The memorandum of association of the company does not show that the principal object for which it was established was one of the objects set out in s. 117. The memorandum makes it clear that no one business activity which the company was authorised to carry on was to be regarded as its principal object to the exclusion of any other. If it can be said that one object rather than another was the principal object that object was to take over and acquire from Campbellfield Holdings the existing business. The words in s. 117 "established for the purpose of carrying on any business" mean that the company must be established for the purpose of carrying on exclusively one or more of the types of business set out in pars. (*a*) to (*e*). That submission is based on the fact that the section is dealing with co-operative companies. Section 118 suggests that a company ceases to be co-operative if one of its principal objects falls outside s. 117. If it is permissible to go beyond the provisions of the articles and memorandum the evidence makes it clear that this business was not established having one of the matters in s. 117 as a principal object. The predominant object was to continue the existing business but in a way which would lighten the burden of taxation. The payment of the sum of £13,000 to the suppliers was merely a payment for goods sold and delivered. The object of ss. 117 et seq. is co-operation in the nature of the constitution of the

(1) (1952) 86 C.L.R. 530.

company [He referred to *Shelley* v. *Federal Commissioner of Taxation* (1).] This case is not within s. 117 (*b*) " the acquisition of commodities or animals from its shareholders for disposal or distribution " because that paragraph on its proper construction is limited to the acquisition of commodities for distribution in the same form as they are acquired. The words " from its shareholders " means from them as an entire class. The decision of the Court in *Ardmona Fruit Products Co-operative Co. Ltd.* v. *Federal Commissioner of Taxation* (2) is correct.

K. A. Aickin in reply.

Cur. adv. vult.

April 30.

The following written judgments were delivered :—

DIXON C.J., WILLIAMS AND WEBB JJ. Section 120 (1) (*b*) of the *Income Tax and Social Services Contribution Assessment Act* 1936-1951 provides that so much of the assessable income of a co-operative company as is distributed amongst its shareholders as . . . dividends on shares shall be an allowable deduction.

In the year of income the appellant company distributed dividends amounting to £12,800 on its A and B class shares and to £38 2s. 0d. on its C class shares. It claimed to be allowed these amounts as a deduction from its assessable income on the ground that it is a co-operative company. That expression is defined for the purpose by s. 117. The most material part of the definition requires that the company shall be established for the purpose of carrying on any business having as its primary object or objects the acquisition of commodities from its shareholders for disposal or distribution or the processing of commodities of its shareholders : (s. 117 (*b*) and (*c*)).

The appellant company manufactures sausage casings from the intestines of sheep and grown lambs. The intestines from which the casings are made are supplied by wholesale butchers, eight in number, who are members of the company holding C class shares. C class shares, of which 635 are issued, carry a preferential dividend of 6 per cent per annum amounting in all to £38 2s. 0d. The A and B class shares which, except in one case, are held by other people, carried in the year in question a dividend of 200 per cent, amounting in all to £12,800.

Because the C class shareholders, who received the dividend of £38 2s. 0d., sold to the appellant company the intestines or runners

(1) (1929) 43 C.L.R. 208, at pp. 226-234.

(2) (1952) 86 C.L.R. 530.

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through the treatment of which and resale as sausage casings it made its profit, the appellant company claims to deduct from its assessable income so much of the profit as it distributed as a dividend upon the A and B class shares, the holders of which supplied nothing. The commissioner has failed to recognise in this a form of co-operation for the encouragement of which the allowance was designed. Hence his refusal to concede the deduction. It is easy enough to agree with the commissioner that the reward of one class of shareholders for the " co-operation " of another class of shareholders was not what the legislature had in mind in framing ss. 117 to 120. But it is quite another thing to find in the text which has actually been written in those provisions for the legislature a clear and convincing reason supplying a logical justification for the *a priori* faith that no such consequence could ever have been intended. It seems all to depend on the definition, contained in s. 117, of the expression " co-operative company ". When the appellant company was formed it is evident that the definition was before those responsible for its constitution and that their desire was to bring it within the shelter of the provision. Yet a rash conservatism led to the perilous inclusion in the memorandum of association of all the customary heterogeneity of objects. The definition imposes several distinct conditions. First the company, if it is to be a " co-operative company " for the purpose of the deduction, must by its rules limit the number of shares which may be held by, or on behalf of, any one shareholder. This the articles of association of the appellant company expressly do. They provide that no number of shares in excess of 5,000 shall be held by or on behalf of any one shareholder of the company. The authorised capital of the company is £10,000, divided into 8,000 A class shares, 1,000 B class and 1,000 C class of £1 each. For the commissioner it is objected that to fix the limit at half the authorised capital is no real compliance with s. 117. But there are the words—" the rules of which limit the number of shares which may be held by, or by and on behalf of, any one shareholder ". No maximum proportion or figure is specified. It is impossible to say that 5,000 out of 10,000 shares is not a limit upon what may be held. Then the rules of the company must prohibit the quotation of the shares for sale or purchase at any stock exchange or in any other public manner whatever. That is done in terms by the articles. A company may be a co-operative company although it has no share capital but, as members and stockholders are included in the definition of " shareholder " (s. 6 (1)), the provisions of ss. 117 to 120 speak throughout of " shareholders ". Section 117 sets out a number of objects any one or

more of which will suffice if it is the primary object, or they are the primary objects, of a business for the carrying on of which the company was established. Notice that it is the object or objects of the business, not the object or objects of the company, to which the section, in terms, refers. Is this an accident and does the section really intend to make the definition turn on the primacy of some object or objects of the company as contained in its memorandum ? In such a provision as that under consideration one cannot be certain that distinctions of language are a safe guide to the draftsman's meaning. But at all events what he has said is " any business having as its primary object or objects ". Further, the difficulties are notorious of any attempt to sort out the objects expressed in a modern memorandum of association and form a judgment as to which matters most or is " primary ".

To say what the primary purpose of a business is may not always be quite easy, but relatively speaking the test it provides may be considered practicable. We are therefore disposed, not only in the general interest but as a matter of meaning, to reject the idea that you should look, at all events exclusively or even initially, at the objects expressed in the company's memorandum.

If one turns to the five lettered paragraphs setting out the " objects " forming the legislature's choice, of which only portion of two has been extracted so far as relevant to this case, and reads them with ss. 118 to 120, it will be seen that the foundation of the allowance of the distributions among shareholders is that the fund distributed is the product of goods or money provided by the shareholders. It would not be unnatural to infer that the class of shareholders mentioned in the lettered paragraphs of s. 117 must be co-extensive with the class among whom the distribution is made for which s. 120 (1) provides. Yet the difficulties of such an interpretation are very great, too great indeed to allow of its acceptance. Complete identity could not be expected. In a large number there would always be some shareholder who failed to use the company. It is obvious too that a disproportion must exist between the shareholding and the contribution of each to the company's profits. Lastly, the proviso to s. 120 (1) clearly enough contemplates the failure of not more than ten per cent of the shareholders to use the company. It seems therefore impossible to read the provisions as requiring that the shareholders receiving the dividend must be co-extensive with the shareholders mentioned in the paragraphs of s. 117. Nor does it seem possible to interpret the provisions as meaning that without being co-extensive the shareholders must belong to the same class. There is nothing in the language which

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gives a foothold for that interpretation. But the words " company which . . . is established for the purpose of carrying on a business having as its primary object or objects " are the all-important words of the provision ; and it is apparent that these words must be read in the closest apposition with the description of objects contained in the respective lettered paragraphs. Each paragraph emphasises the relation of the shareholder to the activity which represents the business. The business must be conducted for performing a particular function for the shareholders. Thus its primary object must be to distribute among them animals or commodities acquired for that purpose or to dispose of such animals or commodities to them. Or it must be to acquire animals or commodities from them for the purpose of disposal or distribution. Or it must be to provide the shareholders with such facilities or requirements as storage, packing, processing or marketing. Or it must be to provide them with services. Finally, there is par. (*e*) concerning loans to them for the purposes specified. The purpose of the business must be to provide the shareholders with these services, facilities or advantages. True it is that the shareholders will obtain these things on a business footing. They will sell or buy the goods, pay for the storage and so on, as any customer would. But it is because the company's business is to render what in a wide sense may be called the services to the shareholders that it is considered proper for it to return the profit to them as dividend etc. without paying tax upon it. That seems to us to be the factor which limits the operation of the wide formula of s. 117 and excludes the present case from it. In the present case there can be no doubt that the company, the appellant company, was established simply for the purpose of carrying on a business of sausage casing manufacture. It was a business which up till that time had been carried on by another company then bearing the same name, a name however which it changed to Campbellfield Holdings Pty. Ltd. when the appellant company took over the business. The appellant company was so established by incorporation in Victoria on 20th July 1949. The old company had allotted shares of a particular class to wholesale butchers from whom the runners were bought. When the appellant company was formed, clearly enough one of the purposes was so to arrange the shareholding that wholesale butchers whence the supplies of runners would be obtained would be shareholders, the hope being that s. 117 would therefore apply. But that is quite a different thing from serving shareholders by acquiring their product. How could it be said that this was the purpose of the business ? Yet what s. 117 demands is a business whose primary object was to do

that or to render some other of the specified services to the shareholders. Neither in the hands of the old company nor in the hands of the new company was the business conducted for the primary object of serving the purposes of the wholesale butchers as shareholders by acquiring the runners forming a by-product of their trade. The dominating motive so it would seem was to earn profits for the holders of A and B class shares. The motive of allotting shares to the suppliers of runners was subordinate even if powerful. No one can doubt that one motive was to obtain the advantage of the allowance or allowances given by s. 120 (1) (*a*) and (*b*). Motive, of course, is not purpose, that is to say it is not necessarily purpose or object. But it seems clear enough that it was not the primary object of the business to acquire the runners from the shareholders of the company or to process their commodities. But for the tax allowance, the runners of any one else would have done as well. Shares were allotted to the suppliers, one may well suppose, because of the benefit to the appellant, if the allowance could thus be obtained. The company's business was not carried on with the object of serving the shareholders who were wholesale butchers, that is, with the object of acquiring their runners for disposal or processing them.

For that reason the claim for the allowance under s. 120 (1) (*b*) fails. The distribution of the so-called bonus or rebate is not in question. Doubtless much might be said for placing that under s. 51 (1). The questions in the case stated should be answered: (1) No; (2) No; (3) Does not arise. The costs of the case stated should be reserved for the judge disposing of the appeal.

FULLAGAR J. This is a case stated by *Kitto* J. in an appeal by a taxpayer company against an assessment of income tax on income derived in the year ended 31st August 1951. The question in the case is whether the company is a "co-operative company" within the meaning of Div. 9 of Pt. III of the *Income Tax and Social Services Contribution Assessment Act*. If it is, it is entitled under s. 120 (1) (*b*) of the Act to deduct from its assessable income of the relevant year a sum of £12,838 paid to its shareholders as dividends on their shares. If it is not a co-operative company, it is not so entitled.

Section 117 of the Act, so far as material, provides that the term "co-operative company" means a company the rules of which limit the number of shares which may be held by or on behalf of any one shareholder, and prohibit the quotation of the shares for sale or purchase at any stock exchange or in any other public

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manner, and which is established for the purpose of carrying on any business having as its primary object the acquisition of commodities or animals from its shareholders for disposal or distribution. A number of other qualifying " primary objects " are mentioned, but this is the only one that I regard as relevant to the present case. Paragraph (*c*) does not, in my opinion, cover cases where the property in the commodity or the animal passes to the company. Section 118, so far as material, provides that if, in the ordinary course of business of a company in the year of income, the value of commodities and animals acquired by it from its shareholders is less than ninety per cent of the total value of commodities and animals acquired by it, that company shall in respect of that year be deemed not to be a co-operative company. Section 120, which, as has been noted, allows a deduction from assessable income of dividends paid by a co-operative company to its shareholders, also allows as a deduction so much of a co-operative company's assessable income as is distributed among its shareholders as rebates or bonuses based on business done by shareholders with the company.

A company named A. & S. Ruffy Pty. Ltd. was incorporated in Victoria in 1933. It has been referred to as the " old company ". It carried on for some years the business of manufacturing and selling sausage casings. It purchased from wholesale butchers, who were the only source of supply, the intestines or " runners " of sheep and lambs, manufactured from these articles sausage casings, and sold the casings so manufactured. Its nominal capital consisted of £5,000 divided into 4,800 "A" shares and 200 " B " shares of £1. The only difference between the "A" shares and the " B " shares seems to have been that only the former carried voting rights. In 1941 the issued capital consisted of 1,440 "A" shares and 160 " B " shares. All the shares were held by members of the Ruffy family. In that year an agreement was reached between the company and three of the wholesale butchers—Townsend, Harris and Thompson—from whom the company obtained its raw material. This agreement provided for a sharing by these three wholesale butchers in the profits of the company, but the plan contemplated was not then carried into effect, because the Treasurer of the Commonwealth refused under the *National Security Regulations* to consent to any issue of new shares by the company.

On 28th February 1946, the articles of the company were amended so as to provide that the capital of the company should be £5,000 divided into 3,600 "A" shares, 400 " B " shares, and 1,000 " C " shares, of £1. On the same day 400 " C " shares were allotted—

170 to Townsend, 130 to Harris and 100 to Thompson. On 9th December 1946 there was a further allotment of 210 " C " shares to certain other wholesale butchers who were suppliers of runners to the company—100 to J. B. Dunn, 50 to Dench Bros., 50 to M. C. Moog and 10 to B. Zmood.

In 1949 there was a reconstruction, which involved the formation of a new company (the taxpayer company) and the winding up of the old company. The first step was to change the name of the old company to Campbellfield Holdings Pty. Ltd. This was done in order that the name "A. & S. Ruffy " might be available for the new company when incorporated. The new company was incorporated on 20th July 1949, under the *Companies Act* 1938 (Vict.). The old company assigned its business and all its assets to the new company in exchange for shares, and then went into voluntary liquidation. The basis of the transaction was that the shareholders in the old company should receive the same number of shares in the new company as they had held in the old company. Some further shares were allotted later.

The nominal capital of the new company was at all material times £10,000 divided into 8,000 "A" shares of £1, 1,000 " B " shares of £1, and 1,000 " C " shares of £1. All shares ranked *pari passu* in a winding up. The rights otherwise attaching to the three classes of shares were thus stated in art. 4 of the company's articles :—" (i) the holders of ' C ' class shares in the capital of the company shall be entitled in priority to all other shares to receive a fixed cumulative preferential dividend at the rate of six pounds per centum per annum on the capital for the time being paid up in respect of such ' C ' class shares ; (ii) subject to the foregoing the directors may from time to time set aside out of the profits of the company in respect of any year or other period such sum as they consider fit for division amongst the members of the company (or some of them in accordance with the provisions herein contained) ; (iii) the directors may notwithstanding any rule of law or equity to the contrary allocate the whole or any proportion of any sum so set aside to, or for payment to or division among, the holders of the ' C ' class shares in the capital of the company (in addition to the preferential dividend payable to the holders of such shares) notwithstanding that the amount available for distribution or division among the holders of the 'A' class and ' B ' class shares is thereby diminished or exhausted : (iv) the directors may notwithstanding any rule of law or equity to the contrary allocate the whole or any portion of the sum so set aside to, or for payment to

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or division among, the holders of 'A' and 'B' class shares notwithstanding that the amount available for distribution or division amongst the holders of 'C' class shares is thereby diminished or exhausted: (v) any sum or proportion of the profits of the company allocated to, or for payment to or division among, the holders of the 'C' class shares in the capital of the company (beyond and in addition to the preferential dividend attaching thereto) shall be divisible amongst the holders of such 'C' class shares in proportion to goods and materials sold and supplied by the holders of such 'C' class shares to the company (during the period in respect of which the sum or proportion of profits is so set aside) and not in proportion to the capital paid up in respect of such share or otherwise. The calculation of the proportions aforesaid shall be based upon the numbers of runners sold and supplied as aforesaid to the company or upon such other basis as the directors shall from time to time determine: (vi) the right (*sic*) attaching to shares in the capital of the company are (subject to the foregoing provisions) as hereinafter set forth in the articles of association; (vii) the directors may from time to time in accordance with the provisions herein contained declare such dividends as they shall think fit: (viii) 'A' class shares only shall confer upon the holders thereof the right to vote at meetings of members of the company and no person who does not hold 'A' class shares shall be entitled to any vote." With reference to sub-par. (vi) above, there are no relevant later provisions in the articles. Article 5 provided:—"(a) Notwithstanding anything to the contrary herein contained or implied no number of shares in excess of 5,000 shall be held by or on behalf of any one shareholder of the company. (b) No shares in the capital of the company shall be quoted for sale or purchase at any Stock Exchange or in any other public manner whatever."

At all material times the issued shares of the company numbered 7,035, of which 5,760 were "A" shares, 640 were "B" shares, and 635 were "C" shares. The "A" shares were held by one Norman Leslie Thompson (2,880) and three other persons. The "B" shares were held by four shareholders. The "C" shares were held by Norman Leslie Thompson (100) and twelve other persons. The only shareholder who held shares of more than one class was Norman Leslie Thompson. In the income year in question the company in the ordinary course of its business acquired more than ninety per cent of the total value of commodities acquired by it from Norman Leslie Thompson and seven other holders of "C" shares, who held among them 225 shares.

In the year in question the company paid to some of its shareholders a " bonus " of £13,155, about which we are not told very much. It was apparently paid to those " C " shareholders who had supplied runners to the company, and would appear to have been allowed by the commissioner as a deduction in his assessment—presumably on the footing that it really represented payment or part payment for goods supplied to the company. If the commissioner was correct in his view of the character of the company, it would not be deductible under s. 120 (1) (*a*). On 7th December 1951, the company resolved that a dividend of 200% on the "A" and " B " shares be paid out of the profits of the year ended 31st August 1951, and that a preference dividend of 6% be paid out of those profits on the " C " shares. The former dividend amounted to £12,800, and the latter to £38. These dividends were in due course paid. In its return the company claimed to deduct the total sum of £12,838 under s. 120 (1) (*b*) of the Act. The commissioner, taking the view that the company was not a co-operative company within the meaning of the Act, disallowed the deduction.

It is clear that the company's rules limit the number of shares which may be held by or on behalf of any one shareholder. It is clear also that they prohibit the quotation of the shares for sale or purchase at any stock exchange or in any other public manner whatever. Two of the three conditions prescribed by s. 117 are thus fulfilled. It is clear also, in my opinion, that the value of the commodities acquired by the company from its shareholders in the ordinary course of its business in the year of income was not less than ninety per cent of the total value of the commodities acquired by it. It is, I think, impossible to find in the words " *its* shareholders " an implication that every shareholder must be a supplier of goods to the company in the year in question. The words may be thought to suggest that what is contemplated is a company all of whose shareholders habitually supply goods to it. But it is at best a vague and dubious suggestion, and it would be very unreasonable that a company should lose its qualification if in any year one or two shareholders happened for any reason not to supply any goods to it, although more than ninety per cent in value of the commodities acquired were acquired from the other shareholders. The condition prescribed by s. 118 must therefore be held also to be fulfilled. The question which thus emerges is whether the third condition prescribed by s. 117 is fulfilled. Is the company a company "established for the purpose of carrying on a business having as its primary object the acquisition of commodities from its shareholders for disposal or distribution" ? In my opinion it is not.

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It would be dangerous, I think, to begin in this case with any *a priori* conception of the *differentia* between a co-operative company and companies generally, and of the reason or reasons for showing favour to such a company in matters of taxation. The only proper course is to take the words of the statute, and inquire whether this company comes within them. The first thing to be noted is that the section speaks of the primary object of the business for the purpose of carrying on which the company is established. We may, of course—and indeed, I think, must—look at the company's memorandum of association, but this cannot be conclusive either way. We must in addition look at the activities actually carried on by the company, and at its history, constitution and control, for all or any of these things may throw light on the purpose of its establishment and the primary object of its business.

The first object stated in the taxpayer company's memorandum is :—" (a) (i) the storage, marketing, taking or processing of commodities of the company's shareholders ; (ii) the rendering of services to the company's shareholders ; (iii) the acquisition of commodities or animals from the company's shareholders for disposal or distribution ; (iv) the acquisition of commodities or animals for disposal or distribution among the company's shareholders." So far we have simply a faithful reproduction of the language of s. 117 with no indication whatever of anything specific that is within the contemplation of the company. But the next two subclauses are specific. The clause proceeds :—" (b) to take over and acquire from Campbellfield Holdings Proprietary Limited the goodwill, land, building and other assets of the undertaking for some time past carried on by the last mentioned company and for that purpose to enter into the agreements referred to in article 3 of the articles of association and carry the same into effect with or without modification ; (c) to carry on the business of casing manufacturers in all its branches ". Then follows a catalogue of miscellaneous objects and powers such as was vainly deprecated in *Cotman* v. *Brougham* (1) : see also *H. A. Stephenson & Son Ltd.* (*In Liq.*) v. *Gillanders Arbuthnot & Co.* esp. per *Dixon* J. (2). The company may do almost anything it likes. So far as sub-cl. (a) is concerned, it would appear that only one of the several activities mentioned was ever contemplated by the company, and the fact that these matters are placed first in the clause affords no reason for saying that any of them constituted the primary object of any business to be carried on. One is certainly disposed, looking at the objects clause as a whole, to infer that sub-cll. (b) and (c) express the real

(1) (1918) A.C. 514.

(2) (1931) 45 C.L.R. 476, at pp. 484-486.

purposes of the company's incorporation, but to say this is not to exclude finally the possibility that the business mentioned may have been intended to have for its primary object something that is mentioned in sub-cl. (a). On the other hand, the miscellaneous list of objects and powers, which follows sub-cl. (c), does not appear to me to throw any light on the question under consideration.

The memorandum is inconclusive. When, however, we look at the history of the company, its constitution, and the activities actually carried on by it, it becomes plain, in my opinion, that the company does not fulfil the third condition prescribed by s. 117. Its predecessor was an ordinary trading company, which in 1946 created a new class of shares—" C " shares—and issued some 600 of them to certain wholesale butchers, who happened to be suppliers of runners to the company. The sole purpose of the creation and allotment of the " C " shares and of the establishment of the new company was to seek the benefit of s. 120 of the *Assessment Act*. This was perfectly legitimate, but it was not a purpose mentioned in s. 117. Neither in the old company nor in the new company had " C " shareholders any rights whatever, while the company was a going concern, except the right to a preferential dividend of six per cent, a trifling sum. Only the "A" shares carried any voting right. The power of appointing directors was in the hands of the "A" shareholders, and the articles gave to the directors the widest discretion as to the distribution of profits. The great bulk of the shares held were "A" and " B " shares, and the "A" shareholders (with one exception) were not suppliers. There was no requirement that " C " shares should be held by suppliers only. All this indicates clearly to my mind that it was a matter of complete indifference (apart, of course, from the desired reduction in taxation) to the company and its "A" and " B " shareholders whether the company bought its runners from one or more or all of the " C " shareholders or from anybody else. The business carried on by the company had no primary object in any relevant sense except to make profits for its "A" and " B " shareholders. It is impossible to maintain that the appellant company fulfils the third requirement prescribed by s. 117.

The first two questions in the case stated should be answered—(a) No : (b) No. The third question does not arise.

TAYLOR J. As appears from the case stated in this matter the appellant company claims that it is a co-operative company within the meaning of Div. 9 of Pt. III of the *Income Tax and Social Services Contribution Assessment Act* 1936-1951 and that so much

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of its assessable income for the year ended 30th August 1951 as was distributed among its members as dividends on shares was an allowable deduction for the purposes of assessing its liability to income tax. The amount in question is £12,838, that being the total of the amounts required to pay dividends which were declared on the different classes of shares which constituted the company's share capital.

The contention that the appellant was a co-operative company rested primarily upon the assertion that it was established for the purpose of carrying on a business having as its primary object the acquisition of commodities from its shareholders for disposal or distribution (see s. 117 (*b*)). It was further asserted that the other conditions prescribed by ss. 117 and 118 were satisfied, namely, that the rules of the company limited the number of shares which might be held by, or on behalf, of any one shareholder, that the quotation of the shares for sale or purchase at any stock exchange or in any other public manner was prohibited by the rules of the company and that the value of the commodities acquired by the company from its shareholders during the year in question was not less than ninety per cent of the commodities acquired by it in that year.

The appellant sought to make its primary contention good, not by reference to the objects specified in its memorandum of association, but by reference to its trading history and to that of an older company, Campbellfield Holdings Pty. Ltd., the business of which the appellant acquired shortly after its incorporation on 20th July 1949. This history, it was said, clearly showed that the new company was established for the purpose of carrying on a business having as its primary object the acquisition of commodities from its shareholders for disposal or distribution.

In argument the appellant sought to distinguish between the *objects* of the company as declared by its memorandum and the *purpose or purposes* for which the company, with those declared objects, was established. In effect, it is said, the declared objects merely operate to define the legal capacity of the company and the purpose or purposes of its incorporation, and of investing it with specified powers, may be established by reference to extraneous matters. The truth is, however, that a memorandum of association is not required to and does not declare the powers of the company to which it relates ; what is required is that a memorandum shall declare the objects of the company, though, it is from a consideration of its objects that the extent of its powers may be deduced.

As Lord *Wrenbury* said in *Cotman* v. *Brougham* (1) : " The objects of the company and the powers of the company to be exercised in effecting the objects are different things. Powers are not required to be, and ought not to be, specified in the memorandum. The Act intended that the company, if it be a trading company, should by its memorandum define the trade, not that it should specify the various acts which it should be within the power of the company to do in carrying on the trade " (2).

The memorandum of the appellant company is not in any unusual form. It expressly declares that the " objects for which the company is formed " are those thereinafter specified. Thereafter are specified a number of activities and it is not out of place to refer to some of them. Among those specified are :—

" (3) (a) (i) the storage, marketing, taking or processing of commodities of the company's shareholders ;

(ii) the rendering of services to the company's shareholders ;

(iii) the acquisition of commodities or animals from the company's shareholders for disposal or distribution ;

(iv) The acquisition of commodities or animals for disposal or distribution among the company's shareholders ;

(b) to take over and acquire from Campbellfield Holdings Proprietary Limited the goodwill, land building and other assets of the undertaking for some time past carried on by the last mentioned company and for that purpose to enter into the agreements referred to in Article 3 of the Articles of Association and carry the same into effect with or without modification ;

(c) to carry on the business of casing manufacturers in all its branches ;

(d) to manufacture, deliver, sell, import, export and deal in and with all kinds of animal, vegetable and mineral products and by-products artificial and natural skins and to carry on business as tallow makers, gut cleaners, fellmongers, tanners, skin, leather and hide merchants, wool scourers, wool brokers, butchers, preservers, canners and the like ;

(e) to erect and manage abattoirs, freezing works, sheds, warehouses, and like buildings and to carry on business

(1) (1918) A.C. 514.

(2) (1918) A.C., at p. 522.

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as exporters, importers, indentors, wholesalers, manufacturers, distributors and agents;

(f) to carry on business as farmers, graziers, sheep, cattle and livestock dealers, station and ranch owners and to purchase, charter, hire, build, or otherwise acquire interests in ships, barges, lighters, carts, cars, trucks, boxes, cases, bottles, casks and all other types of vehicles conveyances and containers;

(g) to carry on business as general merchants, carriers, wharfingers, storekeepers, printers, engineers, carpenters, painters, contractors, decorators, electricians, publishers, grocers, manufacturing chemists, ice merchants and corn, straw and fodder dealers;

(k) to buy sell take on lease licence exchange apply for a grant of or otherwise deal in and with land and purchase acquire hire and dispose of and make contracts relating to any real and/or personal property or interest therein and any patents copyrights formulas secret processes or information concessions trade marks brevets d'invention licences and other like rights and any other rights or privileges which the company may think necessary or convenient for the purposes of its business and to use exercise develop or grant licences in respect of or otherwise turn to account the property rights or information so acquired;"

it is unnecessary to enumerate any others for the instances given are sufficient to show that the objects of the company are both manifold and diverse. Further, it is declared by the memorandum that the objects specified therein shall be construed in the most liberal way and shall in no wise be limited or restricted by reference to or inference from the terms of the first or any other paragraph and none of the objects specified or the powers thereby conferred shall be deemed subsidiary or auxiliary merely to the objects mentioned in the first paragraph.

It will be seen that it is quite impossible to say that the acquisition of commodities from the company's shareholders for disposal or distribution was the primary object of the company and this fact might, in other circumstances, give rise to questions of some difficulty. Can it be said, for instance, that a company with such declared objects could ever fall within the provisions of s. 117? Or, is it permissible to attempt to establish by evidence that the appellant company, with such a constitution, was established for the purpose of pursuing one object rather than another? Or, is the

essential question to be decided merely by considering the character of the business actually carried on by the company during the relevant year of income? It is, however, unnecessary to answer these questions for such evidence as there is in the case is quite incapable of supporting the conclusion on any basis, that the company was established for the purpose of carrying on a business having as its primary object the acquisition of commodities from its shareholders for disposal or distribution.

As already appears the evidence upon which the appellant relies relates to its trading history, particularly during the relevant income year, and to that of the older company, Campbellfield Holdings Pty. Ltd. No doubt, it is true that the appellant acquired ninety per cent or more of its commodities during that year from its C class shareholders and that it distributed practically the whole of its assessable income among its shareholders. But it is apparent that the core of its business was the manufacture of sausage casings from the appropriate raw materials and that by far the bulk of its activities which resulted in profit were to be found in the manufacturing processes which were undertaken. Reference to the manufacturing account for the relevant year shows that manufacturing costs amounted to £25,243 whereas the cost of raw materials used amounted initially to £3,195 though this was supplemented by what were called bonuses, amounting to £13,155, to its member suppliers. Whether these so called bonuses represented payments over and above the market price of the goods supplied does not appear for we were given no information concerning the terms upon which the C class shareholders supplied their goods; it was left for us to speculate whether the C class shareholders supplied raw materials to the company on the basis of receiving a price for their goods calculated by reference to ruling market prices or whether, in return for their goods, they were to receive some proportion of the company's profits whatever they might be.

It appears from the case stated that after payment of the bonuses referred to the company made a net profit for the year in question of £12,840 and out of this sum dividends were paid to the various classes of shareholders. By the articles it was provided (art. 4) that the capital of the company of £10,000 should be divided into 8,000 A class shares of £1 each, and 1,000 each of B class and C class shares of £1 each. At the relevant time 5,760 A class shares had been issued and these were held by four shareholders. The issued B class shares totalled 640 and these were held by a further four shareholders. Of the C class shares 635 had been issued and they were held by thirteen shareholders. One of these shareholders also

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held some A class shares but the remaining twelve held only C class shares. By the articles the holders of C class shares were entitled, in priority to all other shares, to receive a fixed cumulative preferential dividend at the rate of six pounds per cent per annum on the capital for the time being paid up in respect of such shares. Subject to that provision the directors were authorised to set aside out of the profits of the company in respect of any year such sums as they might consider fit for division among members of the company and they were authorised to allocate the whole or any proportion of any sum so set aside for payment to or division among the holders of the C class shares to the exclusion of the holders of A and B class shares and, alternatively, to allocate the whole or any portion of the sum so set aside to or for payment to or division among the holders of A and B class shares to the exclusion of the holders of C class shares. It should be observed that the only shareholders who were entitled to vote at any annual general meeting were the holders of A class shares (art. 54). At the annual general meeting of the company on 7th December 1951 it was resolved that a dividend of 200 per cent on the A and B class shares should be paid from the profits of the year ended 31st August 1951 and that a preference dividend of six per cent should be paid on the C class shares from the profits of the same year. The result was that out of the profits of the company for that year preference dividends, which absorbed £38 of the profits of the year, were paid to the holders of the C class shares. Pursuant to the provisions of the articles, this sum was divisible among the holders of such shares in proportion to the goods and materials sold and supplied by them to the company during the year. The dividends to the holders of the A and B class shares, on the other hand, absorbed £12,800. It will be seen that what actually happened was that the shareholders who supplied goods to the company received by virtue of their C class share holdings token payments by way of dividends and that the holders of the A and B class shares received practically the whole of the profits available for distribution by way of dividend. In other words, the suppliers of raw materials to the company received practically nothing by way of dividend whilst those who were the holders of the A and B class shares received by virtue of their shareholding practically the whole of the net profits. Such a state of affairs seems to be quite inconsistent with the notion that the company was, in any sense of the term, a co-operative company. The essential character of a co-operative company was the subject of review in *Shelley* v. *Federal Commissioner of Taxation* (1), though

(1) (1929) 43 C.L.R. 208.

it should be observed that in deciding that case, the Court was not constrained by any statutory definition such as appears in s. 117 ; the definition of " co-operative company " appearing in s. 20 of the *Income Tax Assessment Act* 1922-1928 applied only for the purposes of sub-s. (1) of that section and had no application to the provision which the Court was called upon to consider. Yet, in considering the submission of the appellant that its activities show that it was established for the purpose of carrying on a business having as its primary object one of the activities specified in s. 117 it is impossible to lose sight entirely of the broad characteristics of a co-operative company. No doubt it is true that the company acquired practically the whole of its raw material from its C class shareholders during the relevant year and it is true that its profits were distributed amongst its members. But is this sufficient to establish that the purpose, or primary object, of its business was the acquisition of commodities from its shareholders for disposal or distribution ; In my opinion the evidence is not only quite insufficient to establish this proposition but, on the contrary, clearly establishes that it was not. What does appear is that the business of the company was, in essence, that of a manufacturer, that it carried on that business for the purpose of making profits and that the profits, when made, were not, and were not intended to be, distributed on any recognisable co-operative basis. It was quite immaterial to the appellant's business whether the necessary raw material was acquired from its C class shareholders or from some other source and the mere fact that it was so acquired during the relevant year falls far short of establishing that this was the primary object of its business. Indeed the true inference from the proved facts is that the acquisition of the necessary raw material from the C class shareholders was but incidental to the manufacturing processes which constituted the core of the company's business and which were carried on substantially with a view to making profits for the benefit of the limited class of shareholders already mentioned.

It was sought by the appellant to counter the effect of these considerations by the suggestion that the C class shareholders received by way of bonuses over and above the market value of the commodities supplied by them approximately half of the profits of the company remaining after the business expenses for the year had been provided for. It appears to be true, as already mentioned, that they received what were called bonuses to the extent of £13,155 but whether this was received as part of the price for their goods or under an arrangement to accept a share of the company's profits as the price of the goods does not appear. That

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being so, there is nothing in this suggestion to displace the conclusion already expressed.

For the reasons given I agree that the questions asked in the case stated should be answered as proposed in the joint judgment.

Questions in the case stated answered:

(1) *No.*

(2) *No.*

(3) *Does not arise.*

Costs of the case stated reserved for the judge disposing of the appeal.

Solicitors for the appellant, *Oswald Burt & Co.*

Solicitor for the respondent, *H. E. Renfree*, Crown Solicitor for the Commonwealth of Australia.

R. D. B.